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No. 06-1041

FILED

FEB 28 2007

OFFICE OF THE CLERK
SUPREME COURT, U.S.

In The

Supreme Court of the United States

BRUCE COMLY FRENCH, Trustee
For The Debtor Estate Of Ernest Bergman
and Shirley E. Bergman,

Petitioner,

v.

STEVE FREY, ANTHEM BLUE CROSS
AND BLUE SHIELD, AND GERMAN
MUTUAL INSURANCE COMPANY,

Respondents.

On Petition For A Writ Of Certiorari
To The United States Court Of Appeals
For The Sixth Circuit

BRIEF IN OPPOSITION

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QUESTION PRESENTED

Whether the Petitioner has presented "compelling reasons" to grant the Petition, where well-settled precedent of this Court provides that: (i) property rights of a debtor's bankruptcy estate under 11 U.S.C. § 541 are defined by state law, and (ii) funds subject to subrogation rights of non-debtor parties created by contract constitute vested property rights which may not be distributed by a bankruptcy trustee to other creditors of the bankruptcy estate?

CORPORATE DISCLOSURE STATEMENT

Pursuant to Sup. Ct. R. 29.6, LOUIS F. SOLIMINE makes the following disclosure:

> Wellpoint, Inc., traded on the NYSE under the symbol "WLP," is the parent corporation of Community Insurance Company dba Anthem Blue Cross and Blue Shield ("Anthem" or the "Respondent") and, as such, owns more than 10% of Anthem's stock.

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RULE

Sup. Ct. R. 10 1

I. INTRODUCTION

A. Summary of Reasons for Denying Petition

The Petition for Writ of *Certiorari* (the "Petition") fails to set forth compelling reasons for the issuance of a writ as required under Sup. Ct. R. 10. As an initial matter, the decision of the United States Court of Appeals for the Sixth Circuit respecting state law property rights does not conflict with any other decision rendered by the United States Courts of Appeals. Indeed, the Courts of Appeal consistently have recognized and respected Congress's decision to utilize state law definitions of property rights in bankruptcy proceedings in the absence of specific provisions in the Bankruptcy Code requiring a different result.

Additionally, contrary to the Petitioner's suggestions, the Sixth Circuit did not decide an important federal question that had not been previously resolved by this Court. Nor did the Sixth Circuit's ruling conflict with any prior decision of this Court. Rather, the Court of Appeals recognized and properly followed well-settled Supreme Court precedent holding that the Bankruptcy Code does not permit a bankruptcy trustee to distribute other people's property – specifically funds subject to the subrogation rights of non-debtor parties – to other creditors of the bankruptcy estate.

The Petitioner, frustrated and displeased with impact of Ohio property law on his tort action, urges the Court to disregard Congress's decision to leave the definition of property rights to state law, overrule well-settled precedent affirming such Congressional prerogative, and adopt instead a novel theory of federal common law property rights – one that would disregard this Court's specific

recognition of non-debtor subrogation rights in bankruptcy. In support of this extraordinary departure from the established rule of law, and as more fully described below, the Petitioner misconstrues decisions of this Court which are inapplicable to the issue presented and feebly attempts to distinguish those directly on point. Consequently, the Petitioner has failed to satisfy his burden of establishing compelling reasons for the issuance of a writ of *certiorari* and, therefore, the Petition should be denied.

B. Supplemental Background Information

As stated in the Petition, prior to filing their bankruptcy petition, the debtors in the underlying bankruptcy case (together, the "Debtors"), were involved in an automobile accident. Their resulting personal injuries required medical treatment, for which Anthem paid on their behalf medical expenses in the approximate amount of $3,000 pursuant to the terms of a health care plan (the "Plan"). Pursuant to the terms of a subrogation clause in the Plan, upon Anthem's payment of those medical expenses, it became vested with a property right in any funds recovered from any tortfeasor up to the amount of its payment (the "Subrogation Claim"). The subrogation clause specifically provides:

> We [Anthem] have the right to recover payments we make on your behalf from any party responsible for compensating you for your injuries. The following apply: We have first priority for the full amount of benefits we have paid from any recovery regardless of whether the payments you receive make you whole for your losses and injuries.
>
> [. . . .]

> You and your legal representative must do whatever is necessary to enable Us [Anthem] to exercise Our rights and do nothing to prejudice them.
>
> [. . . .]
>
> To the extent that the total assets from which a Recovery is available are insufficient to satisfy in full Our [Anthem] subrogation claim and any claim still held by you, Our subrogation claim shall be first satisfied before any part of a Recovery is applied to your claim, your attorney fees, other expenses or costs.
>
> [. . . .]
>
> You and your legal representative must hold in trust for Us [Anthem] the proceeds of the gross Recovery (i.e., the total amount of your Recovery before any attorney fees, other expenses or costs) to be paid to Us immediately upon your receipt of Recovery.

In accordance with this subrogation provision, and corresponding judicial precedent under Ohio law, both the District Court and the Sixth Circuit Court of Appeals determined that funds subject to Anthem's Subrogation Claim were not property of the Debtors' bankruptcy estate under 11 U.S.C. § 541. Indeed, the Petitioner appears to concede that, in a non-bankruptcy context, under Ohio law, Anthem's Subrogation Claim is a vested property right in which the Debtors can claim no interest. Likewise, the Petitioner has not challenged the propriety of the Ohio Supreme Court's interpretation of state law property rights.

Instead, the Petitioner asks this Court to repudiate well-settled precedent holding that property rights – even

in bankruptcy proceedings – are determined according to state law. In place of this long-settled doctrine, the Petitioner invites the Court to create out of whole cloth a "federal definition of property" for purposes of bankruptcy proceedings and, in the process, to disregard this Court's prior recognition and validation of non-debtor subrogation rights. Thus, the central issue is whether the Court is willing to entertain a dramatic departure from prior precedents which affirm that property rights under 11 U.S.C. § 541 are determined by state law and respect rights of subrogation vested in non-debtor parties.

II. REASONS FOR DENYING PETITION

A. Summary of the Argument

For nearly thirty years, this Court has expressly recognized Congressional preference to leave to state law the determination of whether specific property rights are assets of a debtor's bankruptcy estate. *Butner v. U.S.*, 440 U.S. 48 (1979). More specifically, in a situation remarkably similar to the case *sub judice*, this Court ruled that bankruptcy courts must recognize and respect subrogation rights which vested before bankruptcy in persons other than the debtor. *Pearlman v. Reliance Ins. Co.*, 371 U.S. 132 (1962). Ohio law, in turn, recognizes an insurer's property right, arising out of a subrogation provision in an insurance contract, in any recovery from a tortfeasor responsible for the damages suffered by the insured, to the extent the insurer compensates its insured for those damages. *Blue Cross & Blue Shield Mutual of Ohio v. Hrenko*, 647 N.E.2d 1358 (Ohio 1995).

Consequently, unless this Court is prepared to effect a radical change to well-established precedent – notwithstanding

the Petitioner's failure to advance any "special justification" for such an extraordinary measure – it should not expend scarce judicial resources re-examining the decision rendered by the United States Court of Appeals for the Sixth Circuit. In accordance with *Butner* and its progeny, as well as *Pearlman*, the Court of Appeals properly determined that the Petitioner is prohibited from using the bankruptcy process to administer funds in which the Debtors have no property interest.

B. The Petition Fails to Provide Any "Special Justification" to Disregard *Stare Decisis* and Overrule Prior Precedent

This Court has repeatedly emphasized the "fundamental importance" of *stare decisis*, the basic legal principle that requires the Court to respect earlier decisions as well as the rules of law they embody. *Randall v. Sorrell*, 126 S. Ct. 2479, 2489 (2006) citing *Harris v. U.S.*, 536 U.S. 545, 556-57 (2002) (plurality opinion) (citing numerous cases). "*Stare decisis* 'promotes the evenhanded, predictable, and consistent development of legal principles, fosters reliance on judicial decisions, and contributes to the actual and perceived integrity of the judicial process.'" *Randall*, 126 S. Ct. at 2489 quoting *U.S. v. Int'l Business Machs. Corp.*, 517 U.S. 843, 856 (1996) (quoting *Payne v. Tenn.*, 501 U.S. 808, 827 (1991)). To preserve and promote settled legal expectations, the "rule of law demands that adhering to prior case law be the norm." *Id.* In this regard, "[d]eparture from precedent is exceptional, and requires 'special justification,' especially once the precedent has become well-settled "through iteration and reiteration over a long period of time." *Id.* quoting *Arizona v. Ramsey*, 467 U.S. 203, 212 (1984).

In this matter, the Petitioner has failed to provide any "special justification" for overruling *Butner* and its progeny. According to the Petitioner, the statutory amendments to the Bankruptcy Code effected by Congress in 1978 and 2005 "require that the Court be vigilant in reining in lower court decisions that limit Congress's definition [of property of the estate]." However, what the Petitioner fails to recognize is that if Congress had determined that state law property rights should not be utilized for defining property under 11 U.S.C. § 541, then Congress could have overruled *Butner* and its progeny by modifying the Bankruptcy Code to achieve such a result. The absence of any references in the Petition to specific changes to the Bankruptcy Code that would lend support to such a conclusion is telling. The only logical – and obvious – conclusion is that Congress did not so decide, but rather intended property rights to continue to be defined by state law. Congress's nearly three decades of silence on this issue is a powerful and compelling testament to its intentions.

Furthermore, the Petitioner has failed to identify any particular federal law pertaining to a debtor's rights *vis a vis* subrogation that would provide "special justification" for the Court to overrule *Butner* and *Pearlman*. As recognized by *Butner* and noted in the Petition, when Congress enacts federal legislation that pre-empts the field with respect to a particular subject, this Court will interpret the debtor's property rights under the Bankruptcy Code to carry out the purpose of the federal legislation. *See Patterson v. Shumate*, 504 U.S. 753 (1992). Similarly, any state law related to and in conflict with the federal legislation would cede to the federal law under the doctrine of preemption. Given the noticeable absence of any specific

federal legislation overriding the various states' approaches to insurers' subrogation rights and the Court's decision in *Pearlman*, no "special justification" exists for overruling this Court's well-settled precedent with respect to this issue.

C. The Court of Appeals Properly Adhered to the *Butner* Doctrine Which Provides that the Definition of Property Rights Under 11 U.S.C. § 541 is Generally Determined by State Law

Unless a particular federal interest is at issue, this Court has held that property rights are created and defined according to state law. *Butner,* 440 U.S. at 55 (noting Congress's constitutional authority to enact uniform laws of bankruptcy, but also recognizing Congress's choice to generally leave the determination of property rights in the assets of a debtor's estate to state law). In this Court's judgment, "[u]niform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving 'a windfall merely by reason of the happenstance of bankruptcy.'" *Id.* quoting *Lewis v. Mfrs. Nat'l Bank*, 364 U.S. 603, 609 (1961). In accordance with this principle, this Court held that state law applies not only to ownership interests, but also to other property interests as well, including security interests. *Id.*

Despite modifications and enhancements of substantive federal bankruptcy law which have occurred over time, this Court has continued to adhere to the principles of *Butner*, reinforcing the notion that property rights of a debtor's bankruptcy estate are determined by state law.

See Raleigh v. Ill. Dep't of Rev., 530 U.S. 15, 20 (2000) ("Creditors' entitlements in bankruptcy arise in the first instance from the underlying substantive law creating the debtor's obligation, subject to any qualifying or contrary provisions of the Bankruptcy Code"); *Nobelman v. Am. Sav. Bank*, 508 U.S. 324, 329 (1993) ("The term 'rights' is nowhere defined in the Bankruptcy Code. In the absence of a controlling federal rule, we generally assume that Congress has 'left the determination of property rights in the assets of a bankrupt's estate to state law.'"); *Barnhill v. Johnson*, 503 U.S. 393, 398 (1992) (holding that what constitutes a transfer of "property" under 11 U.S.C. § 547 is determined by state law).

Consistent with the legal principles underlying these decisions, the Court of Appeals correctly concluded that the Petitioner did not have any claim to property in which Anthem already had a vested interest through its right of subrogation under Ohio law. *French v. Frey*, 467 F.3d 536 (6th Cir. 2007). The Petitioner has not challenged either current Sixth Circuit precedent or the Sixth Circuit's application of Ohio law, nor has he challenged the propriety of the Ohio Supreme Court's decision concerning insurers' subrogation rights. Accordingly, unless the Court is willing to consider an extraordinary departure from the continued vitality of *Butner*, notwithstanding the absence of any "special justification," the Petition should be denied.

D. The Court of Appeals Properly Applied *Pearlman* by Concluding Anthem's Subrogation Rights Were Not Property Interests of the Debtors' Bankruptcy Estate

Aside from subrogation rights provided by state law, this Court has also held that bankruptcy courts must

recognize and respect subrogation rights which arise before bankruptcy in persons other than the debtor. *Pearlman*, 371 U.S. at 132 (holding that a fund due to the debtor, for which a surety is entitled to reimbursement by subrogation, never becomes a part of the bankruptcy estate). In *Pearlman*, the debtor-construction company, prior to filing bankruptcy, entered into a construction contract with the federal government. *Id.* at 133. As required by statute, the company obtained two surety bonds which, in part, authorized the government to retain and hold a percentage of the payments due to the company until final completion and approval of the work and payment by the company of its obligations to its laborers. *Id.* at 133-34.

Before completing the work, the company terminated the contract, which resulted in another contractor finishing the job. *Id.* The surety company, pursuant to the bond, satisfied the company's obligations to materialmen and laborers. *Id.* The government, recognizing the withheld funds were not government property, paid the funds to the company's bankruptcy trustee. *Id.* The surety company then filed a complaint seeking to recover the funds in the district court, which held that the right of the surety in such circumstances is to be accorded priority over general creditors. *Id.* at 135. After the United States Court of Appeals for the Second Circuit affirmed the decision of the trial court, the trustee appealed its decision to this Court. *Id.* at 135.

In seeking reversal of the Second Circuit's decision, the trustee in *Pearlman* raised an argument nearly identical to the one raised by the Petitioner here, suggesting that the dispute was governed entirely by the Bankruptcy Act (the "Act") and that the Act afforded no priority

to a surety's claim for reimbursement. Rejecting the trustee's position, this Court stated:

> Ownership of property rights before bankruptcy is one thing; priority of distribution in bankruptcy of property that has passed encumbered into a bankrupt's estate is quite another. Property interests in a fund not owned by a bankrupt at the time of adjudication, whether complete or partial, legal or equitable, mortgages, liens, or simple priority of rights, are of course not part of the bankrupt's property and do not vest in the trustee. The Bankruptcy Act simply does not authorize a trustee to distribute other people's property among a bankrupt's creditors.

Id. at 135-36. This Court held that "a surety who pays the debt of another is entitled to all the rights of the person he paid to enforce his right to be reimbursed. This rule is generally known as the right of subrogation." *Id.* at 137.

As the Court of Appeals recognized in the decision below, the recognition and validation of Anthem's subrogation right comports with this Court's decision in *Pearlman. French*, 467 F.3d at 539. Upon Anthem's payment of medical expenses on behalf of the Debtors, Anthem became vested with a property right in the proceeds of any recovery from a tortfeasor liable for the injuries up to the amount of Anthem's payment. Thus, the language in the Plan granting Anthem these subrogation rights, just like the language of the surety bond at issue in *Pearlman*, creates a property interest that accrues to the subrogee alone and which never becomes part of a debtor's bankruptcy estate.

In the face of this daunting obstacle to his case, the Petitioner resorts to an unconvincing attempt to distinguish

Pearlman by suggesting that the Court's decision, despite its unequivocal language, was driven solely by the fact that the project could not have been completed without the bond. However, courts have never read *Pearlman* so narrowly and the Sixth Circuit's decision below represents an accurate reflection of the legitimacy and strength of subrogation rights in or out of bankruptcy proceedings. As a result, the Petition should be denied.

III. CONCLUSION

Petitioner has failed to establish compelling reasons for the Court to grant the Petition. Therefore, Anthem respectfully requests that the Petition be denied.

Respectfully submitted,

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